HUNGARY

In, the U.S. trade deficit with Hungary amounted to $1.1 billion in 1998 (or $493 million more than the deficit in 1997). U.S. merchandise exports to Hungary in 1998 were $482 million, a decrease of approximately $3 million (1 percent) from the previous year. Hungary was the United States' 68th largest export market through November 1998. U.S. imports from Hungary amounted to $1.6 billion in 1998, an increase of $489 million (45.4 percent). U.S. and Hungarian bilateral trade figures differ dramatically due to country-of-origin distinctions in exports. Such distinctions are especially apparent with products whose final assembly occurs in Hungary, particularly computer equipment (estimated $800 million of recorded imports). Although Hungary remains a middle-income country with substantial regional disparities, it has been transformed into a market economy with an elaborate legal and regulatory framework based on those of developed Western economies. U.S. foreign direct investment (FDI) in Hungary from 1989 to the end of 1998 surpassed $6 billion. The total FDI in Hungary during this time consisted of an estimated $18.5 billion. Hungary is a leading recipient of U.S. investment in Central and Eastern Europe.

IMPORT POLICIES

As part of Hungary's transition from a communist to a free-market economy, import policies were liberalized rapidly after 1989 to encourage competition and to allow imports necessary for restructuring. Almost 96 percent (by value) of products can be imported without an import license. A license is required to import precious metals, military goods, and certain pharmaceutical products.

The progressive implementation of Uruguay Round agreements has generally improved U.S. market access to Hungary. Under these agreements, Hungary must eliminate quotas on textiles, clothing, and other industrial products by 2004. As of January 1, 1998, Hungary eliminated their Global Consumer Import Quota with respect to WTO member countries and import quota licenses for WTO member-states' imports of new vehicles with engine capacity greater than 1500 cc, apparel, medicine, used clothes, string and thread, carpets, and those types of radio receivers not produced in Hungary. Import quotas, totaling $408 million in 1998, applied to jewelry, a handful of industrial products, and (for non-WTO members only) apparel and carpets. Only about 60-70 percent of quotas are utilized and in 1998, not one was fully utilized. However, administrative difficulties in securing licenses affected a U.S. footwear firm importing from the Far East.

The Hungarian Government allocated import licenses for up to 68,000 new and 63,000 used cars in 1998. However, these figures are well above the actual number imported. The Customs Duty Law of 1995 forbids the importation of used cars over six years old. Specialized older vehicles may still be imported after passing a technical test. These regulations, combined with standards for used cars which tend to exclude older U.S. models, effectively curb most used car imports from the U.S.

In 1995, Hungary raised many agricultural tariffs to Uruguay Round binding ceilings and introduced numerous tariff-rate import quotas assigned to most-favored nation (MFN) or preferential suppliers.

Hungary's average most-favored nation (MFN) import duties have been cut from 13.6 percent in 1991 to eight percent in 1998, in accordance with its Uruguay Round commitments. Under Hungary's 1991 Association Agreement with the EU, and subsequent accords, tariffs for industrial imports from the EU are being eliminated by the end of 2001. The result has been that many U.S. products are subject to notably higher tariffs than are EU products. By the end of 1998 only about 45 percent of the products originating from the EU remained dutiable. At the beginning of 1999, the tariffs on the remaining industrial products were reduced to 30 percent of the basic duty. By 2001, duties on these industrial products will be abolished entirely. Some tariffs on non-industrial EU products have also been reduced on a selective basis. Several

U.S. exporters (e.g., of aircraft, autos, electrical generating equipment, chocolate and non-chocolate confections, distilled spirits, wine, commercial laundry equipment, and soda ash) have expressed concern over the tariff preferences provided to the EU by Hungary, because of the growing disparity with MFN rates. Hungary applies a high duty of 72 percent ad valorem on imported alcoholic beverages and 30-70 percent ad valorem duties on chocolate and confectionary products. The USITC (United States International Trade Commission) is currently studying the effects of such preferences on U.S. exports. Its findings are due in April 1999.

On January 1, 1997, the government eliminated a two percent statistical fee and one percent customs clearance fee for WTO member states. Fees totaling five percent, however, are still required of goods coming from non-WTO states. Under the Pan-European cumulation system and Pan-European Free Trade Zone, effective in Hungary since July 1, 1997, customs duties on the imported content of goods subsequently exported under preferential trade agreements are no longer refunded. However, content from any member state can accumulate to qualify for preferential treatment. Duties and fees on re-exported content are no longer refunded as of July 1, 1997 for non-EU importers. This change has adversely affected certain U.S. industries (e.g., lumber and veneer producers). Firms exporting from Hungary with inputs from non-WTO members (such as Russia) were faced with greater costs and additional customs fees. An American aluminum processor, for which unrefunded fees would have totaled over $5 million per year, secured an 18-month waiver of these fees in August 1997, but its long-term status remains unclear.

STANDARDS, TESTING, LABELING AND CERTIFICATION

Importers must file a customs document with a product declaration an, present Hungarian certified documentation from the Commercial Quality Control Institute upon importation. This permit may be replaced by other national certification and testing agency documents, such as those of the National Institute for Drugs. Some standards are reciprocal with those of recognized U.S. standards enforcement agencies.

Animal and Plant Health Regulations

Hungarian import regulations limits and delays imports of breeding animals, livestock semen, planting seeds, and new plant varieties. The process of registration and testing of new plant varieties imported is time-consuming and costly. In 1998, U.S. and other exporters of bovine semen secured modification of restrictive practices and fees on imports affecting a potential market of $1 million per year for U.S. firms.

In 1998, Hungary adopted legislation governing genetically-modified organisms (GMOs) in agriculture which, in following EU practice, imposes unnecessary restraints on imports primarily affecting new plant varieties. The Ministry of Agriculture could minimize these restraints with a flexible regulatory regime. Although the market for seed imports is relatively small (est. $18 million in 1998), U.S. firms in Hungary produce seed and plant stock for other markets. Full liberalization of the GMO policy could mean additional U.S. exports in the $10-25 million range.

GOVERNMENT PROCUREMENT

Foreign access to government-funded construction and service or supply contracts is regulated by the 1995 Act on Public Procurement, which improved transparency. Tenders must be invited for the purchase of goods worth over 10 million forints (currently 215 forints equal one dollar). However, bids with more than 50 percent Hungarian content are considered equal to majority-foreign bids that are up to 10 percent lower in price. Purchases deemed to be related to state security, as well as purchases of gas, oil, and electricity, remain exempt from these regulations. Hungary is not party to the WTO Government Procurement Code, and some

U.S. firms have taken legal action against non-transparency and procedural irregularities in government tenders.

EXPORT SUBSIDIES

While Hungary's agricultural export subsidies remain in excess of its WTO commitments, the Hungarian Government is phasing out excess subsidies and has undertaken not to use subsidies to penetrate new export markets (under an October 1997 agreement with the U.S. and other petitioning members of the WTO).

LACK OF INTELLECTUAL PROPERTY PROTECTION

Hungary's intellectual property rights (IPR) laws are adequate in many respects, but significant gaps remain and prosecutorial enforcement needs to be strengthened substantially. Piracy of audiovisual works and computer programs has decreased, but remain extensive. Copyright legislation also needs to provide for retroactive protection of U.S. works, civil *ex parte* search provisions, and refined pipeline protection for patents.

Patent Protection

Hungarian patent protection was strengthened following the conclusion of a comprehensive U.S.-Hungary bilateral agreement on IPR protection in 1993. Under this agreement, Hungary agreed to protect pharmaceutical products, unlike the previous law in which patents were limited to processes for producing pharmaceuticals. The bilateral IPR agreement provides transitional pipeline protection for U.S. pharmaceutical products otherwise ineligible for new product patents in Hungary, patent rights application regardless of whether products are imported or locally produced, and limitations on the use of compulsory licenses. Implementation of this legislation began on July 1, 1994.

There are, however, limitations to Hungary's Pipeline Protection Law that make pipeline protection inadequate under certain circumstances. For example, no pipeline protection can be obtained for products where a corresponding foreign counterpart patent is issued after the effective date of Hungary's Pipeline Law (i.e., after July 1, 1994). The Pipeline Protection Law also entails the uncertainty that a Hungarian company, once an invention is published, may have started work to develop a corresponding product before the innovator can file their pipeline application. Under such circumstances, it appears that a patent holder could then not enforce the pipeline patent. There is also a problem with Article 20 of the new law, in addition to the incorrect application of the "modification of priority" concept.

Persistent problems in the Hungarian judicial system continue to hinder protection of patent rights. In 1997, the Hungarian Government strengthened access to legal injunctions and attempted to reduce the backlog of court cases. However, this action did not affect ongoing IPR disputes, including a long-standing patent infringement suit by a large U.S. pharmaceutical firm. U.S. interests have not been able to obtain injunctive relief prohibiting the marketing of products that the courts have deemed infringing. The lack of relevant technical expertise in the courts can result in patent infringement cases taking three or more years to reach conclusion. Penalties awarded in such cases are considered too low to act as effective deterrents.

Copyright Protection

Hungarian copyright laws largely conform to international standards, but certain legislative steps still need to be taken before they meets bilateral IPR and TRIPs commitments. The 1993 bilateral IPR agreement recognizes an exclusive right to authorize the public communication of work, including to perform, project, exhibit, broadcast, transmit, retransmit or display. The agreement also requires that protected rights be freely and separately exploitable and conferrable (contract rights), as well as recognizing an exclusive right to authorize the first public distribution including importation for protected works. To meet its TRIPs obligations, Hungary still needs to provide full retroactivity for sound recordings and civil *ex parte* search provisions. Encrypted signals must also be protected by prohibiting unauthorized retransmission of signals, the manufacture, distribution, possession, sale, rental and use of unauthorized descrambling devices. In early 1999, the Hungarian Government appeared likely to approve a new copyright law which would address several of these gaps.

In May 1993, Hungary added stiff penalties for copyright infringement to its penal code. Since then, piracy of audiovisual works and transmissions has been driven underground and remains high. Overall, prosecutions of audiovisual piracy are steady at about 200 per year. In December 1998, the courts issued a landmark verdict against a pre-release video piracy ring, sentencing 11 persons to a combined 16 years of imprisonment.

Nonetheless, fines remain too low even for a middle-income country (total fines assessed in 1997 were HUF 1.5 million, or approx. $8200). The U.S. motion picture industry estimates that 55-0 percent of videotapes circulating in 1998 were pirated (down from 85 percent in 1993). Of the roughly 1200 cable broadcasting systems in Hungary, 30 percent regularly make unauthorized transmissions of videos, and retransmission of descrambled cable and satellite signals. The total annual loss from audiovisual piracy in 1998 is estimated at $19 million.

Under current law, employers are prevented from exercising all economic rights with respect to software created by employees. This law deters foreign and local investment in software development and publishing.

SERVICES BARRIERS

Public television is required to fill 70 percent of its air time with European production and 51 percent of which must be Hungarian, excluding advertising, news, sports, game and quiz shows. Hungarian film quotas in the 15 to 20 percent range apply to public television. These quotas are not seen as cutting actual U.S. market share. For private broadcasters, the 1995 Media Law reserves 10 percent of program time for Hungarian programs, excluding films (increasing to 15 percent after January 1, 1999). In selling licenses for two private national television frequencies in 1997, the National Radio and Television Board (ORTT) mandated a European quota of 50 percent of total annual program time, excluding ads, news, sports, and game shows (Hungarian content quotas apply as well). However, U.S. feature films and television productions retain a strong presence, especially in prime time.

Sales of U.S. air and ground services in Hungary are limited, since the U.S. and Hungary do not have a bilateral "Open Skies" civil aviation agreement.

Legal Services

Hungary introduced new restrictions on foreign lawyers and law firms under legislation passed in 1998, which requires *inter alia* that foreign legal practitioners associate with a Hungarian firm or lawyer. The law's provisions are compounded by new restrictions proposed by the Hungarian Bar and by difficulties in securing tax identification. Some U.S. law firms in Hungary believe the restrictions could significantly reduce market access for U.S. legal services.

A person cannot provide foreign legal consultancy services nor legal advice on foreign or international law without being licensed in the practice of Hungarian law. Foreigners in legal firms can establish themselves; however all employees must be Hungarian.

Architecture and Engineering Services

Only Hungarian nationals may be licensed as architects and engineers.

Accounting Services

Audits must be conducted by Hungarian-certified accountants. Such individuals may work for foreign firms.

INVESTMENT BARRIERS

Hungary's commitment to cash privatization of large state enterprises has made it a leading recipient of foreign direct investment, especially U.S. investment, in Central and Eastern Europe. Hungarian Governments have progressively reduced state ownership in "strategic" enterprises from 50 percent to 25 percent to a single golden share with veto rights.

Government delays in approving energy price increases have repeatedly prevented U.S. and other foreign firms from realizing the eight-percent returns guaranteed in energy privatization contracts. In December 1998, the Hungarian Government announced price increases effective January 1999, but the issue will remain unresolved until foreign investors and the government agree on a new regulatory framework and pricing mechanisms for the energy sector.

Since 1994, Hungary has offered targeted tax incentives for investment (replacing blanket incentives) based on export promotion, reinvestment of profits, and job creation in areas of high unemployment. More recent tax incentives target investment to depressed areas of the country, chiefly the northeastern Hajdu-Bihar, Nograd, Borsod-Abauj-Zemplen and Szabolcs-Szatmar-Bereg regions. In 1998, the government implemented a 10-year corporate tax break to companies investing at least HUF 10 billion, creating 500 or more jobs. If the investment takes place in an economically distressed region, the minimum investment is HUF 3 billion.

A customs law, passed in late 1995, eliminated duty-free importation of capital goods by foreign-owned companies. The law, intended to place domestic enterprises on an equal footing with foreign-owned competitors, eliminated a prior incentive to invest in Hungary.

ANTICOMPETITIVE PRACTICES

Privatization and entry into the Hungarian market for most multinationals has greatly increased competition in most sectors. However, some key infrastructural monopolies (broadcast transmitter Antenna Hungaria, electricity wholesaler MVM, state railways MAV, and two-thirds of Malev airlines) remain state-owned and receive special consideration from the Hungarian Government. In the telecommunications sector, the awarding of monopoly phone concessions (including to U.S.-owned firms) during privatization has delayed the introduction of full competition until December 31, 2003. Hungary has committed as part of the WTO Basic Telecom Services Agreement to allow unlimited competition in the telecom sector starting on that date.

ELECTRONIC COMMERCE

Sales via the Internet are unrestricted, but subject to taxation. Internet purchases of physical goods are subject to customs duties and value-added tax (VAT) if delivered from abroad or from within Hungary. The Customs Office assesses and collects VAT on software imported on physical media and/or installed on hardware. No customs duty payment is required in case of buying software purchased and delivered via the Internet, however, VAT should be paid after the purchase (on a self-assessment basis).

OTHER BARRIERS

Although bribery is seldom seen to penetrate the highest levels of the Hungarian state, transparency remains an issue in business dealings. Some U.S. firms complain of inappropriate influences in government tenders.

The U.S. distilled spirits industry believes Hungary's excise taxes discriminate against imported whiskey, vodka, rum and liqueurs in favor of domestically produced fruit brandies and eaux de vie, in violation of GATT Article III, paragraph 2.

Many firms operating in Hungary are caught unaware by shifts in government policy due to insufficient government consultation with business interests. In other cases, the exceptional autonomy of the judicial system and of the National Radio and Television Board (both products of Hungary's transition to democracy) sometimes leads to decisions inconsistent with an overall government policy of promoting economic openness. In addition, complaints have been registered with the U.S. Government concerning inconsistent implementation of customs regulations and procedures when exporting to Hungary.